S&P Global Ratings

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Denver City & County, Colorado Denver International Airport; Airport

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Denver City & County, Colorado
Denver International Airport; Airport

Credit Profile		
US$255 mil arpt sys rev bnds (Denver Intl Arpt) ser 2017A due 11/15/2023		
Long Term Rating	A+/Stable	New
US$21.2 mil arpt sys rev bnds (Denver Intl Arpt) ser 2017B due 11/15/2033		
Long Term Rating	A+/Stable	New
Denver City & Cnty, Colorado		
Denver Intl Arpt, Colorado		
Denver City & County (Denver International Airport)		
Long Term Rating	A+/Stable	Affirmed
Denver City & Cnty Dept of Aviation, Colorado		
Denver Intl Arpt, Colorado		
Denver City & County Department of Aviation (Denver International Airport)		
Long Term Rating	A+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'A+' long-term rating to Denver City & County, Colo.'s series 2017A and series 2017B airport system revenue bonds issued for Denver International Airport (DIA). At the same time, S&P Global Ratings affirmed its:

- 'A+' long-term ratings and underlying ratings (SPUR) on DIA's outstanding senior-lien general airport revenue bonds, and
- 'A' long-term ratings and SPURs on DIA's outstanding subordinate-lien bonds.

The outstanding debt was issued for DIA by Denver City & County and Denver City & County Department of Aviation, Colo. The outlook on all ratings is stable.

The department is issuing the pro forma $255.0 million series 2017A bonds and pro forma $21.2 million series 2017B revenue bonds to currently refund all or a portion of its series 2007A, 2007C, and 2007D airport system revenue bonds. The pro forma bonds carry a fixed interest rate and a final maturity date of Nov. 15, 2033, matching final maturity on the refunded bonds. The series 2017A and 2017B bonds are secured by a senior-lien pledge of airport system net revenues.

The ratings reflect our view of DIA's credit strengths, which include:

- The continued commitment from United Airlines to operate a major hub at DIA, as evidenced by the long-term use and lease agreement and significant level of enplanements and continued connecting activity;
- Strong passenger traffic levels, driven by a growing origin and destination (O&D) passenger base, with 2016 enplanements hitting record levels for the third consecutive year, and our expectation that strong growth will be sustained in the near term with modest positive growth over the longer term;

- A strategic location for the east-west flow of domestic traffic and no major competing facilities within 500 miles;
- Strong liquidity levels, with unrestricted cash and investments consistently amounting to over 500 days' operating expenses, and that we expect will be sustained at or greater than 500 days' cash on hand; and
- Excellent airfield efficiency and significant capacity for future growth, with six runways and more than 50 square miles of land.

In our opinion, the preceding credit strengths are partially offset by:

- A very large growth-driven capital improvement plan (CIP) that includes additional bonding plans we expect will likely pressure debt service coverage (DSC) levels over the next five to eight years;
- The inherent vulnerability associated with moderately high concentration in one airline, with United (including United Express) representing about 42% of passenger traffic; and
- A moderately high debt burden, which we expect will continue to rise as a result of debt-financing of continued capital needs over the intermediate term.

In recent years, DIA has experienced strong and increasing enplanement levels, particularly among the top two carriers, United Airlines and Southwest Airlines. Supporting this trend is, in our view, the Denver metropolitan area's strong economic and population growth trends in recent years, in addition to United's long-term commitment to maintaining DIA as a hub. While steady growth has supported strong margins that translate to consistently strong DSC and liquidity levels, another result has been that certain airport facilities are operating at or above design capacity. Thus, DIA has commenced a major CIP--$3.5 billion over five years, 2018-2022--that will entail the largest gate expansion since the airport opened in 1995, a redevelopment of the landside terminal, and several other projects intended to expand and improve airport facilities. While the CIP presents significant challenges to management, and we expect DSC and other metrics may be pressured as a result of a rising debt burden, we believe DIA's management team will manage these pressures.

At fiscal year-end 2016, the airport had about $3.9 billion in total debt outstanding. Debt per enplanement is moderately high, in our opinion, at $134 at fiscal year-end 2016. With the additional borrowing plans at DIA, we expect debt per enplaned passenger will increase to closer to $200 while total debt outstanding will increase to over $6.6 billion over the next four to five years, contingent upon planned borrowings, those identified in the airport's plan of finance to support its CIP, occurring.

Outlook

The stable outlook reflects our expectation that enplanement levels will remain strong, a result of DIA's strong and growing O&D passenger base in addition to United's commitment to maintaining DIA as a hub, and that liquidity levels will remain strong. The airport's ability to prudently implement its capital plan while maintaining adequate coverage metrics remains an important rating factor.

Upside scenario

We do not expect to raise the ratings during the two-year outlook period, due to our expectation that additional debt issued to support the airport's CIP will pressure DSC and increase leverage.

Downside scenario

Significant additional debt for capital projects that results in materially weaker financial metrics may result in a lower rating.

Airport Facilities

DIA is owned by the city and county of Denver. The city's department of aviation manages and operates the system, per city charter. The CEO of the department of aviation is appointed by the city's mayor. The airfield includes six runways, one of which is the longest commercial service precision-instrument runway in North America. The passenger terminal complex includes a landside terminal and three airside concourses with a total of 111 mainline contact gates and 32 ground loading positions. The terminal and concourses are connected by an underground automated guideway transit system. The airport's concessions span more than 196,000 square feet of retail space and include approximately 190 locations inside the airport. The airport maintains two parking structures adjacent to the terminal building providing nearly 16,000 parking spaces. More than 27,000 additional parking spaces are provided in both close-in and remote surface parking lots.

CIP

Several projects associated with the airport's 2018-2022 five-year CIP will expand and modify airport facilities. The projects included within the airport's $3.5 billion CIP primarily result from the long-term trend of rising enplanement levels, as higher enplanement levels pressure the airport's facilities and necessitate capacity-related expansions and updates. Management's plan of finance identifies approximately $3.2 billion (90% of the total CIP) of project costs to be funded with the proceeds of additional bonds. Per management, the entire CIP will be reviewed at least annually, with project financing to be adjusted as plans change, whether due to changes in projected enplanement levels or other factors.

A major gate expansion included in the five-year CIP will add 39 gates to DIA, a 35% increase in total contact gates and the largest gate expansion since the airport opened in 1995. The gate expansion program includes additions to each of the three concourses. The program carries a total estimated cost of $1.5 billion and includes related airfield and repaving projects. Construction is slated to begin in 2018, with gates scheduled to open by 2021.

The CIP also includes $479 million in airport funds that will be applied to the Jeppesen Terminal Great Hall Program, a public-private partnership with a total estimated of $650 million. The Jeppesen Terminal project entails the redevelopment of levels 5 and 6 of the landside terminal, an area totaling about 1 million square feet. Under the terms of the partnership, the airport will finance about $479 million of development expenses and retain 80% of concession revenues postcompletion, with the remainder flowing to the developer. Upon completion, estimated to be November 2021, the city will make annual supplemental payments to the developer. These payments will be treated as junior-lien obligations under the bond documents, and we include these obligations as debt-like payment in our evaluation of forecast DSC. DIA's agreement with the developer, Denver Great Hall LLC, runs to 2051.

Under internal policy, management evaluates capital investment decisions in the context of the effects such investments will have on three primary metrics: DSC, days' unrestricted cash on hand, and cost per enplanement (CPE). We believe such policies reflect favorably on management's fiscal prudence, and we consider management's track record strong, as demonstrated by financial performance and operational stability. In our view, management's approach to planning and budgeting is a credit strength.

Use And Lease Agreements

DIA has use and lease agreements with all major domestic carriers and foreign-flag carriers providing service at the airport. The airport has agreements with carriers other than United Airlines through 2018. The airport has two one-year options to extend the agreements beyond 2018. The United Airlines agreement expires in 2035. The United agreement includes a hub commitment under which United will maintain operations at DIA proportionate to its nationwide system, and the airline will pay financial penalties if it does not comply with the terms of the agreement. Overall, we consider this agreement to be a credit positive as it evidences United's commitment to maintaining the airport as a hub. All of the use and lease agreements utilize a hybrid rate-setting methodology, calculating landing fees under a cost center residual methodology and terminal rental rates under a commercial compensatory methodology.

Demand

DIA ranked as the sixth-busiest airport in the U.S. based on passenger traffic, in 2016, according to Airports Council International. Twenty five airlines provide nonstop service to 190 destinations. DIA's passenger levels have increased significantly in recent years, and the longer-term trend is one of steady increases. At over 29.1 million enplanements in 2016 (7.9% growth over the prior year), enplanements reached record levels for the third consecutive year, and 2017 year-to-date data indicate 2017 will be another record year, with annual growth between 4% and 6%.

Management is forecasting 3.5% growth in 2018 based on announced schedule changes and increases in seat capacity. Thereafter, management projects annual growth of about 1.8-2.0% per year. Although we note that future enplanement growth is uncertain, we believe management's projections are reasonable, given, in particular, United's commitment to DIA and the airport's strong and growing O&D base.

O&D passengers totaled 63.6% of total enplanements in 2016. Since 2010, when O&D passengers constituted 54.2% of the total, the share of O&D traffic has steadily increased. We believe this is largely associated with strong economic and population growth in the Denver metro area, and we view the increasing proportion of O&D traffic as a positive trend, as connecting traffic is inherently more prone to volatility.

United Airlines, together with its affiliate United Express, consistently accounts for a predominant share of total enplanements at DIA. United's share of total enplanements equaled 42% in each of 2015 and 2016, and this share was stable during the first nine months of 2017. DIA is United's fourth-busiest hub in terms of total enplaned passengers. Southwest accounted for 29% of 2015 and 2016's enplanements, and its market share has steadily increased as the airline added capacity and expanded its number of markets served through DIA. Although Frontier Airlines' service levels have fluctuated in recent years, partially due to alterations to its business model, DIA remains Frontier's largest hub. Frontier enplaned 12% of DIA's total passengers in each of 2015 and 2016. Although we note that DIA has heightened exposure to United, due to United's large market share at the airport, we consider United's commitment to operating DIA as a hub as a mitigating factor.

Finances

The airport's financial performance has been strong, in our view. Per our calculations, all-in DSC totaled 1.3x in each of fiscal 2016 and 2015. All-in DSC calculated per the indenture, excluding customer facility charge (CFC) revenues, was 1.6x in 2016, down from 1.8x in each of the four prior years; the drop was primarily a result of higher debt service obligations on the subordinate lien.

Management's financial forecast is reasonable, in our view. The forecast assumes modest annual enplanement growth beyond stronger growth based on announced schedule changes set for 2018, general market stability, and conservative pricing assumptions for planned borrowings. Our calculations, applied to the financial forecast, indicate DSC will fall between 1.2x and 1.3x through fiscal 2020. Thereafter, the forecast indicates DSC may fall to about 1.1x.

In calculating DSC, the indenture allows for the inclusion of rolling coverage from a coverage account. Management's presentation of gross revenues available to pay debt service also includes revenue that is credited back to airlines but subordinate under the flow of funds as gross revenues. Under the indenture, revenues from $3.00 of the $4.50 passenger facility charge (PFC) levied in that year offset the annual debt service obligation. The remaining $1.50 PFC revenue is designated for debt service payments and included as gross revenues under the indenture, and we understand that management intends to use designated PFC revenue to pay debt service on senior bonds. Although CFC revenues are included as gross revenues under the bond ordinances, management has prudently presented DSC exclusive of CFC revenues, both historically and in its financial forecast, because it plans to potentially apply CFCs to support construction of a rental car facility in the future.

Our DSC calculations exclude rolling coverage and revenue credited back to the airlines. In calculating DSC, we apply all PFC revenues applicable to debt service as gross revenues--we do not apply any offsets to debt service--and exclude CFCs from available revenues. Under management's presentation of DSC and ours, the metrics include all senior-, subordinate-, and junior-lien obligations, and thus reflect all-in DSC.

Liquidity is consistently a credit strength for DIA. Including unrestricted cash, cash equivalents, and unrestricted investments, total liquidity of $736.8 million in fiscal 2016 equated to 573 days' operating expenses, per S&P Global Ratings' calculation. Management maintains a liquidity target of 500 days' cash on hand. Management's plan of finance for its CIP includes cash-funding certain capital expenditures. As a result, we expect available liquidity to fall closer to 500 days' cash on hand through fiscal 2022--a level we still consider supportive of the current rating.

We view DIA's airline cost structure moderate. CPE, per our calculations, was $11.99 in 2016. According to the financial forecast, CPE will likely remain steady trough 2018, before rising as additional debt associated with the CIP pushes annual expense requirements higher. Although we expect CPE will rise over the next five years, we do not believe a rising CPE will materially weaken DIA's strong competitive position.

Contingent Liquidity

Based on our criteria, we consider DIA's contingent liability risk to be low. DIA has 18 outstanding swaps (with 8 counterparties). The airport also has several direct purchase obligations. As of Nov. 1, 2017, the combined notional amount of these swaps was approximately $1.3 billion, with a negative mark-to-market valuation of $98.9 million. The airport is not required to post collateral unless the senior-lien rating falls below 'BBB'. A termination rating trigger under these swaps for the airport occurs if the senior-lien rating falls below 'BBB'. We consider the possibility of this as remote, given the differential between the current and trigger ratings. We consider the contingent liability risk related to these swaps and direct purchase obligations manageable. We have reviewed the terms and provisions of the direct purchase obligations, and we do not believe these pose material contingent liquidity risk to the airport.

Issuer/Obligor

Denver International Airport is owned by the City and County of Denver. City charter delegates management and operation of the system to the city's department of aviation. The manager of the department of aviation is appointed by the city's mayor.

Bond Provisions

We consider the bond provisions to be credit neutral. The bond provisions remain unchanged under the supplement ordinance associated with the series 2017 bonds. A pledge of net airport revenues, after the payment of operating and maintenance (O&M) expenses, secures the senior-lien bonds. Further securing the senior-lien bonds is a consolidated debt service reserve, funded at maximum annual debt service. The subordinate bonds are secured by a series-by-series debt service reserve fund, funded to the standard Internal Revenue Service limit.

The flow of funds is typical for airports, in our view, with provisions to pay O&M expenses, senior-lien bonds, bond reserve requirements, and subordinate bond requirements, as well as to fund the O&M reserve account (funded to one-sixth of the previous year's O&M expenses). Excess funds flow to a capital fund. Once deposited to the capital account, funds flow to a coverage account and then an equipment and capital outlay account. At that point, remaining funds flow to the airline revenue credit account, where, per the terms of the use and lease agreements, 50% of the remaining funds are credited to airlines, up to a cap of $40 million per year. The final remaining balance is deposited to a capital improvement account.

The legal provisions include an additional bonds test (ABT) with historical and projected tests. The department may issue additional senior-lien airport system revenue bonds if the following conditions are met:

- Net revenues, including permissible transfers from other available funds, during a 12-month period in the previous 18 months must be at least 1.25x senior-lien debt service for that period, and
- Projected net revenues for each of the three fiscal years after project completion, including transfers from other available funds, must be at least 1.25x aggregate debt service on all outstanding and proposed senior-lien bonds.

The subordinate-lien ABT includes a 1.10x multiple.

Ratings Detail (As Of November 22, 2017)		
Denver City & Cnty, Colorado		
Denver Intl Arpt, Colorado		
Denver City & Cnty (Denver International Airport) (Term Rate-AMT)		
Long Term Rating	A+/Stable	Affirmed
Denver City & Cnty (Denver Intl Arpt) arpt sys rev bnds (Denver Intl Arpt)		
Long Term Rating	A+/Stable	Affirmed
Denver City & Cnty (Denver Intl Arpt) sr arpt sys rev bnds (Amt)		
Long Term Rating	A+/Stable	Affirmed
Denver City & Cnty (Denver Intl Arpt) sr arpt sys rev bnds (Non-Amt)		
Long Term Rating	A+/Stable	Affirmed
Denver City & Cnty (Denver Intl Arpt) AIRPORTS		
Long Term Rating	A+/NR/Stable	Affirmed
Unenhanced Rating	NR(SPUR)	Current
Denver City & County Department of Aviation (Denver International Airport) (AGM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Denver City & County (Denver International Airport) (AMT)		
Long Term Rating	A+/NR/Stable	Affirmed
Unenhanced Rating	NR(SPUR)	Current
Denver City & Cnty Dept of Aviation, Colorado		
Denver Intl Arpt, Colorado		
Denver City & Cnty Dept of Aviation (Denver International Airport) subord (AGM)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Denver City & Cnty Dept of Aviation (Denver Intl Arpt) arpt sys subord rev bnds (AMT) (Denver Intl Arpt)		
Long Term Rating	A/Stable	Affirmed
Denver City & County Department of Aviation (Denver International Airport) (wrap of insured) (MBIA, National & ASSURED GTY) (SEC MKT)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Denver City & County Department of Aviation (Denver International Airport) (AMT) (MBIA) (BHAC)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Denver City & Cnty Dept of Aviation (Denver Intl Arpt)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Denver City & Cnty (Denver Intl Arpt) arpt sys		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.